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TAGS: ECON ETRD EINV EIND PREL KPAO CA
SUBJECT: CANADA'S LIST OF TRADE IRRITANTS CEMENTING IDEA OF GROWING
U.S. PROTECTIONISM

Refs: (A) Toronto 85 (B) Toronto 98
(C) Ottawa 160

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¶1. (SBU) Summary: Several recent U.S.-Canada trade irritants have led Canadian business associations and the media to accuse the USG of economic protectionism. The major problem areas are the Country of Origin Labeling (COOL) voluntary requirements on meat products and "Buy American" provisions in federal stimulus legislation. Other events, such as recent U.S. duties on softwood lumber, the USG elevation of Canada to the Special 301 Priority Watch List, "Black Liquor" tax breaks for U.S. pulp paper producers, and the looming June 1 implementation of the Western Hemisphere Travel Initiative, have reinforced the negative perception here of the United States on economic matters. End summary.

Canadians Doubting Top-Level Assurances

¶2. (SBU) During his visit to Canada in February 2009, President Obama stated, "My administration is committed to making sure that even as we take steps to strengthen the U.S. economy, that we are doing so in a way that actually over time will enhance the ability of trading partners, like Canada, to work within our boundaries." Prime Minister Harper similarly opined: "If we start thinking simply nationally and start having policies that try and restrict the benefits only within our borders and try and implement protectionist measures, this will not have the effect we need to have on the global economy, and it's the global economy that's pulling most of us down." Despite the top-level commitments to keep markets open, Canadian business associations and media charge that the United States has instituted protectionist measures against Canada.

Buy American

¶3. (SBU) The Buy America provisions of the American Recovery and Reinvestment Act (ARRA) exclude Canada and other U.S. trading partners from supplying iron, steel, manufactured goods, and many other products for state and municipal projects financed by ARRA funds. Although the NAFTA provides reciprocal market access by a

number of federal agencies, no market access commitments exist at the sub-federal level. The Association of Canadian Manufacturers and Exporters states that as a result of the ARRA, Canadian firms are having their orders cancelled by U.S. purchasers - including Federal entities such as Department of Defense elements that are covered by the language on international trade commitments - or are being asked to sign affidavits to verify that they are supplying only U.S.-made products to government purchasing agents at the sub-state level. Even Canadian goods destined for projects not funded by the ARRA (or non-manufactured goods permitted under the ARRA) are being refused by sub-federal procurement officers not wanting to potentially run afoul of the ARRA's Buy America restrictions, according to Embassy contacts. One case that has received extensive Canadian press coverage involved the removal of newly-installed, Canadian-made sewage pipe at the Camp Pendleton Marine Base, reportedly for fear of violating the Buy America provisions. The pipe came from a Canadian subsidiary of the Belgian Qprovisions. The pipe came from a Canadian subsidiary of the Belgian IPEX company. In several other cases that we have heard of, the affected exporter is actually a Canadian subsidiary of an American firm.

¶4. (SBU) Comment: It is true that Canadian provinces were offered the opportunity during the original NAFTA negotiations seventeen years ago to agree on reciprocal "most-favored-entity" treatment from 37 U.S. states. The Canadian provinces missed that boat. That being said, however, the sectors on offer from these 37 states in many cases were very limited and would not have covered many of the sectors that today are being affected by the ARRA. The remaining 13 U.S. states, including some of Canada's largest trading partners, were not willing to come to the table. End comment.

¶5. (U) The extension of Buy America provisions to other U.S. legislation (such as the Water Quality Investment Act) has provoked fears in the Canadian business community that Buy America provisions will become a standard component of U.S. appropriation and authorization legislation. One Canadian community, Halton Hills, Ontario (refs A, B) has responded by declaring that it will only make municipal purchases from suppliers in countries that do not impose local trade restrictions. While this small suburb of Toronto lacks market power on its own, it has asked the other 1774 members of the Canadian Federation of Municipalities to follow suit. The Federation will decide on the resolution in June.

¶6. (SBU) Beyond possible retaliation by Canadian municipalities against U.S. goods, Buy America has had effects on U.S. enterprises that are upstream suppliers for Canadian firms. For example, the multi-billion dollar U.S.-Canada market for water and wastewater equipment is highly integrated with suppliers servicing contracts on both sides of the border. U.S. and Canadian governments have allocated billions of dollars in new spending for municipal water and sewer upgrades. Given the highly interlinked nature of the U.S.-Canadian economic relationship, by closing off cross-border supply chains, Buy America will likely negatively affect U.S. firms. IPEX (whose products were removed from Camp Pendleton) buys about 90 percent of its chemical inputs, valued at more that $170 million per year, from American suppliers, particularly in Texas and New Jersey. Hayward Gordon, a pump and mixer manufacturer from Halton Hills, expects to lose 30 percent of its sales this year as a result of Buy America. This will have direct effects on its Wisconsin-based supplier of gearboxes and its Georgia-based supplier of electric motors.

COOL

¶7. (U) The voluntary components of U.S. Country of Origin Labeling rules has raised concerns among Canadian meat producers - especially the requirement to provide disaggregated information about an animal's place of birth, feeding and slaughter (see ref C for details). The regulations (including the voluntary measures) went into effect on March 19, 2009. They preempt an earlier agreement reached with Canada and Mexico that would have permitted Made in

North America labeling.

¶8. (U) Similar to the industrial sectors affected by Buy America, COOL is also having a negative impact on U.S. agri-business because of the highly integrated status of the North American beef and pork industries. For example, hogs that are born in one country are frequently raised and slaughtered in the other. COOL voluntary measures ask meat processors, retailers, etc. to process and label this mixed origin product separately. As a result, U.S. feeding operations and processing plants are losing business. Nearly ten percent of hogs slaughtered in the United States are of Canadian origin. Most imported Canadian hogs are processed at U.S. Midwest pork plants. Ron Plain, an agriculture economist at the University of Missouri estimates that at least one U.S. Midwest pork plant will have to close because, without the Canadian stock, U.S. pork plants Qhave to close because, without the Canadian stock, U.S. pork plants will not have enough hogs to operate efficiently.

¶9. (U) To avoid penalties for country of origin labeling mistakes, U.S. beef and pork companies are either refusing or segregating cattle and hogs born outside of the United States. Cargill, JBS SA, Hormel Foods Corp, Seaboard Corp and Smithfield Foods, which together sell more than 50 percent of U.S. pork, have either stopped buying Canadian hogs or have announced plans to phase out such purchases. According to the USDA FAS there has been a 42 percent reduction in Canadian hog exports to United States and 1000 fewer hog farms (down from 8300) compared to a year ago.

¶10. (SBU) In early May, Canada and Mexico announced plans to jointly launch a WTO complaint against the United States over COOL. (Comment: Ironically, this action coincided with joint efforts by

Agriculture Secretary Vilsack and Canadian Agriculture Minister Ritz to keep Asian and European pork markets open to North American products in the wake of the H1N1 flu outbreak. End Comment) Canada exports roughly $3 billion in hogs and cattle to the United States yearly, part of more than $10 billion in agricultural sales Canada buys about $14 billion in US-made food products.

Other Concerns

¶11. (U) The USG tax credit for pulp and paper operations using so-called "black liquor" as a power fuel source has also provoked Canadian allegations of unfair industry subsidies. A byproduct of the wood pulp manufacturing process, black liquor has long been used as an energy source for the pulp and paper industry. When mixed with a small amount of diesel fuel, companies burning black liquor for power generation can qualify for a U.S. tax credit designed to encourage the substitution of hybrid sources for fossil fuels. With black liquor tax credits estimated by some Canadian industry analysts to run as high as $4 billion in 2009, there is talk in Canada and the European Union about launching a subsidies challenge against the United States in the WTO

¶12. (SBU) Comment: Both Buy America and COOL are having direct effects on cross-border trade as well as indirect effects that are the result of companies who simply stop dealing with traditional NAFTA suppliers to avoid the hassle of new regulatory regimes. These measures are causing severe disruptions to established and profitable NAFTA supply chains. Many of these disruptions are affecting American businesses and American economic interests. Meanwhile, softwood and black liquor complaints represent some of the more predictable bumps in the cross border trading relationship. However, when combined with the more profound effects of COOL and Buy America, within the highly-charged environment of a global economic crisis, the sum of these problems is greater than the parts and may foster public discontent over the future and utility of NAFTA trading relations. End Comment

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